ROYAL LONDON
ASSET MANAGEMENT

Bond crash dragged equities lower

Q3 2022 review

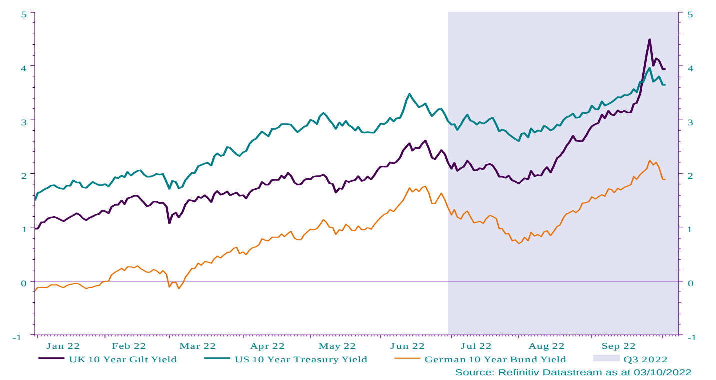
Q3 was extremely volatile for asset class returns. The quarter had started well for risk assets, with stocks experiencing their best beginning to a third quarter in over 50 years. However, as inflation data continued to surprise on the upside, it didn't take long for markets to revert back to their recent downtrend. Stock markets finished at their lowest levels since November 2020 as recession worries, hawkish policy expectations, geopolitics and panic around UK policy saw volatility spike towards the end of the quarter.

High inflation prints and reconfirmation from central bankers that tighter policy would be needed to bring about price stability saw government bond yields turn higher from August. Bonds sold off even further late in September as the UK government unveiled plans for fresh fiscal stimulus; UK 10-year gilt yields moved to 4%, climbing above US 10-year treasury yields for the first time since 2014 (Chart 1). Forced selling by leveraged pension funds resulted in an unprecedented spike in real yields until the Bank of England intervened. The pound also suffered as investors grew nervous on UK assets, which, against a background of continued US dollar strength, saw the currency briefly sink to its weakest ever level versus the greenback (Chart 2).

Year to date commodities have been the strongest asset class for sterling-based investors, while stocks and bonds have both fallen sharply. Bonds have fallen more than stocks, with the strong US dollar offsetting some of the losses in global equities (Table 1).

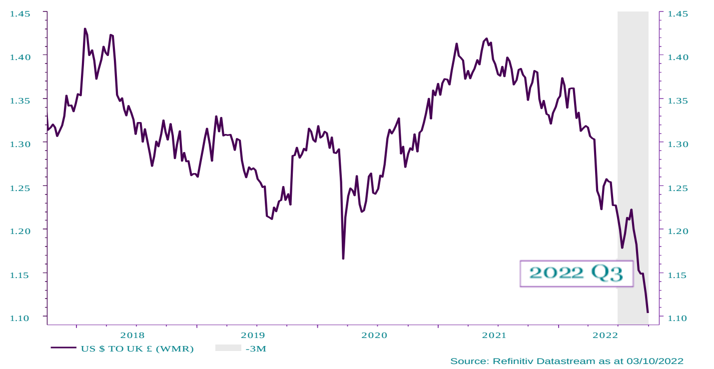
Our tactical asset allocation added value in our funds over the quarter. We have been defensively positioned, underweight stocks and bonds, while favouring more defensive equity regions and sectors. Our preference for the US dollar over sterling also added to performance. Please see the Investment Clock blog for our latest views.

Chart 1: 10 year treasury, bund and gilt yields



Source: Refinitiv DataStream as at 30/09/2022

Chart 2: GBP USD spot rate



Source: Refinitiv DataStream as at 30/09/2022

Table 1: Sterling-based annual returns from major asset classes 2011-2022

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	YTD
1	Gilts +15.6%	EM Stocks +12.8%	Global Stocks +21.2%	Property +19.5%	Property +13.9%	EM Stocks +35.4%	EM Stocks +21.1%	Property +7.5%	Global Stocks +22.6%	Global Stocks +14.3%	Commodities +28.3%	Commodities +37.8%
2	Property +8.1%	UK Stocks +12.3%	UK Stocks +20.8%	Gilts +13.9%	Global Stocks +4.4%	Commodities +33.3%	Global Stocks +14.0%	Cash +0.6%	UK Stocks +19.2%	EM Stocks +11.9%	Global Stocks +20.0%	Property +7.6%
3	Multi Asset +1.0%	Global Stocks +12.1%	Property +11.0%	Global Stocks +12.2%	Multi Asset +1.1%	Global Stocks +30.3%	UK Stocks +13.1%	Gilts +0.6%	EM Stocks +15.9%	Gilts +8.3%	Property +19.9%	Cash +0.5%
4	Cash +0.6%	Multi Asset +6.9%	Multi Asset +6.6%	EM Stocks +7.9%	UK Stocks +1.0%	UK Stocks +16.8%	Property +11.2%	Multi Asset -1.6%	Multi Asset +9.2%	Multi Asset +3.4%	UK Stocks +18.3%	Multi Asset -1.6%
5	UK Stocks -3.5%	Gilts +2.7%	Cash +0.5%	Multi Asset +5.9%	Gilts +0.6%	Multi Asset +12.8%	Multi Asset +6.3%	Global Stocks -3.1%	Gilts +6.9%	Cash +0.3%	Multi Asset +9.2%	EM Stocks -7.1%
6	Global Stocks -6.9%	Property +2.3%	Gilts -3.9%	UK Stocks +1.2%	Cash +0.5%	Gilts +10.1%	Gilts +1.8%	Commodities -5.7%	Commodities +3.5%	Property -1.0%	EM Stocks +1.0%	UK Stocks -7.9%
7	Commodities -12.7%	Cash +0.6%	EM Stocks -5.3%	Cash +0.5%	EM Stocks -10.3%	Property +2.6%	Cash +0.3%	EM Stocks -7.6%	Property +2.1%	Commodities -6.1%	Cash +0.0%	Global Stocks -9.5%
8	EM Stocks -18.4%	Commodities -5.4%	Commodities -11.2%	Commodities -11.8%	Commodities -20.3%	Cash +0.4%	Commodities -7.1%	UK Stocks -9.5%	Cash +0.7%	UK Stocks -9.8%	Gilts -5.2%	Gilts -25.1%

Past performance is not a reliable indicator of future results. Source: RLAM, DataStream as at October 2022; property as at September 2022. 'Multi Asset' returns are based on the benchmark weights of Royal London Global Multi Asset Portfolio (GMAP) Growth Fund / Governed Portfolio 5. Indices used are FTSE All Share, FTSE World, MSCI Emerging Markets ESG Leaders, MSCI/AREF UK All Balanced Quarterly Property Fund, Bloomberg Commodity Index, BoAML BB-B Global Non-Financial High Yield Constrained Index, iBoxx Sterling Non-Gilt Index, FTSE Actuaries UK Index Linked Gilts, Bloomberg Barclays UK Government Inflation Linked Bond 1-10 year Index, Bloomberg Barclays World Government Inflation Linked Bond (ex UK) 1-10 year, FTSE Actuaries UK Conventional Gilts Index, FTSE Actuaries UK Conventional Gilts up to 5

Years Index, SONIA. Total returns in sterling terms.

Markets: The everything sell-off

- Global equity markets ended lower for the third consecutive quarter, the first time this has happened since the global financial crisis. Concerns about recession and tighter policy weighed on sentiment following on from an early summer bounce.
- Government bonds also extended declines as central banks across the globe raised interest rates and hinted of steeper hikes yet to come in order to beat persistently high inflation. Yields moved higher in late September as the UK government unveiled plans for fresh fiscal stimulus.
- Local returns of UK and Japanese stocks continued to benefit from currency weakness. Emerging market shares were weighed down by concerns around Chinese growth and a stronger US dollar.
- Commodities also weakened (in USD terms), experiencing their worst quarter since 2020 Q1, as recession fears grew.
- Sterling fell to its weakest ever level versus the US dollar towards the end of the quarter, as investors reacted to the government's fiscal plans.

FX	1 GBP buys	%chg Q3 (vs GBP)	%chg YTD
USD	1.12	9.0	21.1
EUR	1.14	2.0	4.4
CHF	1.10	5.5	11.9
JPY	161.6	2.3	-3.6
AUD	1.75	1.0	6.8
CAD	1.55	1.4	10.7

CB rates	Rate (%)	chg in Q3 (%)	chg YTD (%)
Fed	3.25	1.50	3.00
BoE	2.25	1.00	2.00
ECB	0.75	1.25	1.25
BoJ	-0.07	-0.03	-0.06

Bond Yield	Yield (%)	chg in Q3 (bps)	chg YTD (bps)
US 10 Year	3.83	82	232
UK 10 Year	4.09	186	312
EU 10 Year	2.11	77	229
JP 10 Year	0.24	1	17

	Local Currency		GBP	
Multi Asset	Q3	YTD	Q3	YTD
UK Stocks	-3.5	-7.9	-3.5	-7.9
Global ex UK Stocks	-4.8	-21.9	1.6	-9.5
Gilts	-12.9	-25.1	-12.9	-25.1
UK Cash	0.3	0.5	0.3	0.5
UK Property	-1.8	7.6	-1.8	7.6
Commodities	-4.1	13.6	4.3	37.8

	Local Currency		GBP	
Equity Regions	Q3	YTD	Q3	YTD
UK	-3.5	-7.9	-3.5	-7.9
North America	-4.7	-24.2	3.5	-8.3
Europe ex UK	-4.7	-21.3	-2.3	-17.0
Japan	-1.2	-5.9	0.9	-9.2
Pacific ex Japan	-5.4	-17.2	-3.3	-11.1
Emerging Markets	-7.7	-19.2	-2.2	-7.1

	Local Currency		GBP	
Global Equity Sectors	Q3	YTD	Q3	YTD
Consumer Discretionary	-0.9	-27.7	5.8	-16.4
Industrials	-3.2	-19.8	2.3	-9.9
Financials	-3.1	-15.7	2.5	-3.8
Consumer Staples	-4.1	-10.2	1.7	2.4
Utilities	-5.7	-8.4	0.3	5.5
Healthcare	-5.5	-13.3	1.2	1.0
Energy	1.6	22.2	7.4	38.2
Materials	-3.9	-16.7	0.6	-7.3
Communication Services	-13.1	-8.8	-8.6	1.7
Technology	-6.0	-32.6	1.0	-20.7

	Local Currency		GBP	
Bonds	Q3	YTD	Q3	YTD
Conventional Gilts	-12.9	-25.1	-12.9	-25.1
Index Linked Gilts	-9.3	-29.3	-9.3	-29.3
GBP Credit	-11.0	-22.2	-11.0	-22.2
Global High Yield	-1.2	-16.1	-1.5	-16.6

	Local Currency		GBP	
Commodities	Q3	YTD	Q3	YTD
Energy	-5.4	49.8	3.0	81.8
Agriculture	-0.2	12.8	8.6	36.9
Industrial Metals	-7.3	-16.2	0.9	1.7
Precious Metals	-7.6	-11.7	0.5	7.2

Note: Standard indices sourced from DataStream and Bloomberg as at October 2022; Property data as at September 2022.

Investment risks – RL GMAP fund range

Investment risk: The value of investments and any income from them may go down as well as up and is not guaranteed. Investors may not get back the amount invested.

Credit risk: Should the issuer of a fixed income security become unable to make income or capital payments, or their rating is downgraded, the value of that investment will fall. Fixed income securities that have a lower credit rating can pay a higher level of income and have an increased risk of default.

Derivative risk: Derivatives are highly sensitive to changes in the value of the underlying asset which can increase both fund losses and gains. The impact to the fund can be greater where they are used in an extensive or complex manner, where the fund could lose significantly more than the amount invested in derivatives.

EPM Techniques: The fund may engage in EPM techniques including holdings of derivative instruments. Whilst intended to reduce risk, the use of these instruments may expose the fund to increased price volatility.

Exchange Rate risk: Changes in currency exchange rates may affect the value of your investment.

Interest Rate risk: Fixed interest securities are particularly affected by trends in interest rates and inflation. If interest rates go up, the value of capital may fall, and vice versa. Inflation will also decrease the real value of capital.

Emerging Markets risk: Investing in emerging markets may provide the potential for greater rewards but carries greater risk due to the possibility of high volatility, low liquidity, currency fluctuations, the adverse effect of social, political and economic instability, weak supervisory structures and accounting standards.

Counterparty risk: The insolvency of any institutions providing services such as safekeeping of assets or acting as counterparty to derivatives or other instruments, may expose the fund to financial loss.

Fund investing in Funds risk: The fund is valued using the latest available price for each underlying investment, however it may not fully reflect changing stockmarket conditions and the fund may apply a 'fair value price' to all or part of its portfolio to mitigate this risk. In extreme liquidity conditions, redemptions in the underlying investments, and/or the fund itself, may be deferred or suspended.

Liquidity and Dealing risk: The fund invests indirectly in assets that may at times be difficult to value, harder to sell, or sell at a fair price. This means that there may be occasions when you experience a delay in being able to deal in the fund, or receive less than may otherwise be expected when selling your investment.

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